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No. 09-1187

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

DEANNA McBREARTY and MARYLYNN HARTSEL, individually, derivatively, and on behalf of all others similarly situated,

Petitioners,

v.

THE VANGUARD GROUP, INC., GEORGE U. SAUTER, DUANE F. KELLY, JOHN J. BRENNAN, CHARLES D. ELLIS, RAJIV L. GUPTA, AMY GUTMANN, JOANN HEFFERNAN HEISEN, ANDRE F. PEROLD, ALFRED M. RANKIN JR., J. LAWRENCE WILSON, ACADIAN ASSET MANAGEMENT, LLC, RONALD D. FRASHURE, JOHN R. CHISHOLM, BRIAN K. WOLAHAN, MARATHON ASSET MANAGEMENT, LLP, NEIL M. OSTRER, VANGUARD INTERNATIONAL EQUITY INDEX FUNDS, d/b/a VANGUARD EUROPEAN STOCK INDEX FUND, and VANGUARD HORIZON FUNDS, d/b/a VANGUARD GLOBAL EQUITY FUND,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

REPLY BRIEF

THOMAS I. SHERIDAN, III
Counsel of Record
ANDREA BIERSTEIN
HANLY CONROY BIERSTEIN
SHERIDAN FISHER & HAYES, LLP
112 Madison Avenue
New York, NY 10016-7416
(212) 784-6404
tsheridan@hanlyconroy.com
abierstein@hanlyconroy.com

Attorneys for Petitioners

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I. Reasonably Foreseeable Intervening Causes Do Not Insulate Racketeers from Civil Liability Under RICO

Respondents' own arguments demonstrate the urgent need for the Court to issue guidance concerning when intervening causes are sufficient to supersede a racketeer's liability under RICO. Respondents contend that Petitioners cannot satisfy proximate causation under RICO because their investment losses were the result of the law enforcement crackdown – and not Respondents' illegal investments – as if a RICO "chain of causation" could have only a single link. (Resp. Br. at 8, 16-17) To the contrary, Petitioners' losses were caused by both Respondents' illegal investments and the law enforcement crackdown. Had there been no crackdown, there might have been no losses. But had there been no illegal investments in the first place, there certainly would have been no losses.

By making the illegal investments, Respondents took a reasonably foreseeable risk that the mutual funds they managed would suffer losses if the government enforced the law. The illegal investments were therefore the primary and efficient cause of the losses, and law enforcement was merely a contributing cause. Law enforcement was not a superseding cause under RICO because it was part of the reasonably foreseeable risk that Respondents' racketeering created. *See, e.g., Bridge v. Phoenix Bond & Indem. Co.*, 553 U.S. 639, 128 S. Ct. 2131, 2144 (2008); *Hemi Group, LLC v. City of New York*, 130 S. Ct. 983, 998 (Jan. 25, 2010) (Breyer, *J.*, dissenting).

The caselaw, in both RICO and antitrust contexts, demonstrates that where, as here, wrongdoing is a material cause of injury, reasonably foreseeable contributing causes do not break the chain of causation. As Circuit Judge Straub observed in a majority opinion joined by then-Circuit Judge Sotomayor, "[a] contrary rule would effectively require that a plaintiff's injury be caused by only one source, and, as this is often not the case, it would operate to insulate from liability defendants who scheme with others in violation of RICO." *City of New York v. Smokes-Spirits.Com, Inc.*, 541 F.3d 425, 442-43 (2d Cir. 2008), *rev'd on other grounds*, 130 S. Ct. 983 (Jan. 25, 2010).

Respondents attempt to distinguish the Court's unanimous decision in *Bridge*, because, according to Respondents, *Bridge* "did not involve intervening causes." (Resp. Br. at 2) That is incorrect. In *Bridge*, the government, relying on the petitioners' misrepresentations, granted more liens to petitioners and fewer to respondents. The Court held that respondents' alleged injury – the loss of valuable liens – had been "the direct result" of petitioners' fraudulent representations to the government. The Court said, "[i]t was a foreseeable and natural consequence of petitioners' scheme to obtain more liens for themselves that other bidders would obtain fewer liens." 128 S. Ct. at 2144.

The Court explained that:

> the complete absence of reliance may prevent the plaintiff from establishing proximate cause. Thus, for example, if the [government] knew

> petitioners' attestations were false but nonetheless permitted them to participate in the auction, then arguably the [government's] actions would constitute an *intervening cause* breaking the chain of causation between petitioners' misrepresentations and respondents' injury.

Id. (emphasis added). Because the government had acted without knowledge of the fraud, however, its foreseeable actions in granting fewer liens to respondents did not even arguably break the chain of causation.

Thus, *Bridge* involved an intervening cause: the government's action in giving fewer liens to respondents. Like the present case, however, *Bridge* did *not* involve a *superseding* intervening cause because the government action had been the "foreseeable and natural consequence" of the defendants' wrongdoing.

Respondents do not dispute that the Court often looks to its antitrust proximate cause precedent for guidance in RICO cases. Nor do they deny that those cases confirm that reasonably foreseeable intervening events do not insulate wrongdoers from liability. Their brief nevertheless ignores those decisions.

Respondents implicitly concede that Petitioners have correctly stated the common law of superseding intervening causes.[1] They do not deny that the decision below is inconsistent with well-established common law

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1. Supreme Court Rule 15(2).

be absolved from liability merely because other causes have contributed to the result, since such causes, innumerable, are always present"). *Accord Blue Shield of Virginia v. McCready*, 457 U.S. 465, 480 n.17 (1982) (antitrust); *Zenith Radio Corp. v. Hazeltine Research, Inc.*, 395 U.S. 100, 114 n. 9 (1969) (antitrust); *Williams v. Mohawk Indus., Inc.*, 465 F.3d 1277, 1288 n. 5 (11th Cir. 2006) (RICO); *Hasbrouck v. Texaco, Inc.*, 842 F.2d 1034, 1042-45 (9th Cir. 1987) (RICO).

Applying well-established common law rules concerning intervening causes, the courts have – without a single exception of which Petitioners are aware – consistently rejected efforts by negligent parties to evade liability on the basis that their wrongdoing was not the sole cause of harm. There is no good reason why racketeers should be treated with greater solicitude than parties who have merely been negligent. There is nothing in the language of RICO to hint of such a limitation.

Respondents acknowledge that *Hemi* fails to provide authoritative guidance to the lower courts because of the lack of a majority opinion. No good can come of Respondents' suggestion that *Hemi* be allowed to "percolate in the lower courts" (Resp. Br. at 14) before the Court resolves the conflict.[3] Further delay in resolving

3. Respondents apparently seek to invoke the Court's "practice of letting issues 'percolate' in the 50 States in the interests of federalism." *Johnson v. Texas*, 509 U.S. 350, 379 (1993) (O'Connor, J., dissenting). The interests of federalism have no application where, as here, the uniform interpretation of a federal statute like RICO is at issue. This practice should also not restrain the Court from resolving uncertainty surrounding an important issue for which the Court sought unsuccessfully to provide authoritative guidance.

these important questions will only benefit racketeers at the expense of victims as the statute of limitations expires on meritorious claims.

II. Courts May Not Disregard The *Holmes* Factors in Favor of a Mechanical Test

Respondents concede that other Circuits have held that proximate causation under RICO should be determined on a case-by-case basis using the *Holmes* factors. Respondents argue, however, that the decision below does not conflict with those decisions because the Second Circuit merely failed "to include in its summary order a detailed analysis" of the *Holmes* factors. (Resp. Br. at 2; *see id.* at 9) That is not a fair characterization of what the Court of Appeals did.

The Court of Appeals assumed for purposes of its decision that all three *Holmes* factors weigh in favor of a finding of proximate causation. Nevertheless, the Court of Appeals considered itself at liberty to disregard them, and to apply its own alternative black letter rule, to reach the opposite conclusion. This case does not present any issue whether the Court of Appeals correctly, albeit *sub silentio*, applied the *Holmes* factors. Rather, this case presents the question whether the Court of Appeals was free to ignore all three factors and rely on an alternative test based on *In re Am. Express Co. S'holder Litig.*, 39 F.3d 395 (2d Cir. 1994), that neither the Court nor any other Court of Appeals has ever approved or followed.

Implicitly recognizing that their first argument will not withstand scrutiny, Respondents argue that the *Holmes* factors weigh in their favor. (Resp. Br. at 17-18) They are wrong. If the *Holmes* factors weighed in Respondents' favor, the Court of Appeals would have simply said so and affirmed on that basis. The court did not do so because what this Court said in unanimously finding proximate causation in *Bridge* is equally true of this case:

> [H]ere, unlike in *Holmes* and *Anza*, [1] there are no independent factors that account for [Petitioners'] injury, [2] there is no risk of duplicative recoveries by plaintiffs removed at different levels of injury from the violation, and [3] no more immediate victim is better situated to sue. Indeed, [Petitioners and the Nominal Defendants whose interest they seek to represent] were the only parties injured by [Respondents' predicate acts].

Bridge, 128 S. Ct. at 2144.

Respondents contend that gamblers who lost money or legal gambling companies (as competitors) can be counted on to vindicate the law. However, gamblers and gambling companies suffered entirely separate injuries from the mutual funds. They do not have standing to seek redress for the injuries suffered by mutual funds and their investors. Moreover, while gamblers and competitors may claim to have been injured by the *operation* of the illegal gambling companies, they have not suffered more direct injury than Petitioners with respect to the relevant racketeering activity alleged in

the complaint: Respondents' investments in illegal gambling businesses in violation of 18 U.S.C. § 1955. Petitioners are the only parties who can be counted on to vindicate the rights of the mutual funds (and their investors).

Instead of applying *Holmes*, the Second Circuit applied a black-letter rule based on its 1994 decision in *American Express*. In that case, the court said that "the commission of the RICO violations was not what injured American Express. Rather, it was the *exposure* of those acts that caused the appellants' harm." 39 F.3d at 399-400 (emphasis added). The court below described *American Express* as extending to cases involving "exposure or *disclosure*" of predicate acts. (4a) (emphasis added)) Implicitly conceding that the injury here was the result of neither "exposure" nor "disclosure" of their racketeering, Respondents seek to expand the rule to cases involving "*interruption* of the predicate acts." (Resp. Br. at 12 (emphasis added)) Whether this ill-defined and ever-expanding rule applies to exposure, disclosure, or interruption of Respondents' racketeering, it has no application to this case.

A primary and recurring source of error in the lower courts' decisions, and in Respondents' brief, is a failure properly to identify the relevant racketeering activity alleged in the complaint. The racketeering predicate acts here are Respondents' investments in illegal gambling businesses in violation of § 1955. Respondents premise their arguments on the assumption that law enforcement "exposed" or "interrupted" their racketeering. (Resp. Br. at 7, 8 & 12) To the contrary, while the law enforcement that contributed to the

investment losses may have "interrupted" *the gambling companies'* illegal activities, it did not expose, disclose, or interrupt *Respondents'* racketeering.

The complaint does not allege that the share prices of the illegal gambling companies fell because Respondents' investments in them were somehow "exposed or disclosed." Nor does it allege that the stock prices fell because Respondents' racketeering activities were "interrupted." Rather, the complaint alleges that the stock prices of the gambling companies fell after U.S. law enforcement successfully choked off the gambling companies' source of illegal revenue. There is absolutely no relationship whatsoever between Petitioners' losses and any exposure, disclosure, or interruption of Respondents' predicate crimes.

Thus, Petitioners' complaint was dismissed on the basis of a bad rule that does not even apply.

III. The Injuries of Which Petitioners Complain Fall Within the Scope of the Predicate Statute

Respondents argue that Petitioners' injuries fall outside the scope of § 1955. (Resp. Br. at 15) That Respondents may have an alternative argument (which the Court of Appeals did not consider) is not a good reason to refuse review of the issues that the court below decided erroneously. The Court generally does not consider such alternative arguments where, as here, they are outside the scope of questions presented in the petition for certiorari and the Court of Appeals did not consider them. *See Roberts v. Galen of Va., Inc.*, 525 U.S. 249, 253-254 (1999) *(per curiam).*

In any event, Respondents' argument is unfounded. Section 1955, which prohibits ownership of "all or part of an illegal gambling business," was enacted together with RICO as part of the Organized Crime Control Act of 1970, Pub. L. 91-452, 84 Stat. 922 (the "OCCA"). The statement of findings that prefaces the OCCA expressly refers to "harm to innocent investors" and the corruption of "legitimate businesses" in connection with "syndicated gambling." 84 Stat. 922-923. Petitioners (innocent investors) and the mutual funds (legitimate businesses that Respondents corrupted) were harmed by Respondents' investments in illegal syndicated gambling. The injuries of which Petitioners complain thus fall well within the set of risks that Congress sought to prevent.

IV. There Is No Exception in § 1955 for Ownership of Illegal Gambling Businesses Whose Shares Are Traded on Foreign Exchanges

Respondents argue that passive, minority ownership of shares of illegal gambling businesses traded on a foreign stock exchange cannot possibly violate § 1955. (Resp. Br. at 14) Once again, the Court need not address this alternative argument because it is outside the scope of questions presented, and the Court of Appeals did not consider it.

In any event, Respondents' argument lacks merit. Section 1955(a) is clear and unambiguous. Whoever "owns all or part of an illegal gambling business" commits a felony. There is no exception for minority owners, passive owners, or illegal gambling businesses whose shares are traded on a foreign stock exchange. The Court should create no such exceptions.

In *Sanabria v. United States*, 437 U.S. 54, 70 n.26 (1978), the Court said, "[n]umerous cases have recognized that [§ 1955(a)] proscribes any degree of participation in an illegal gambling business, except participation as a mere bettor." The complaint here alleges that Respondents caused the mutual funds to participate in illegal gambling businesses as part owners – a form of participation expressly prohibited by the statute.

Respondents argue that ownership of minority interests ought to be exempted. (Resp. Br. at 14) This argument disregards the plain language of the statute, which prohibits owning "all or part" of an illegal gambling business.

Respondents contend that § 1955(a) should be read to exclude passive ownership. The terms "conducts", "manages", "supervises", and "directs" are sufficiently comprehensive to include all forms of active participation. By adding the terms "owns" and "finances" in the statute, Congress prohibited passive financial participation as well as active participation.

Respondents claim that Petitioners' view of Section 1955 "would make a felon out of anyone who purchases a minimal interest in a publicly owned gambling company . . . ." (Resp. Br. at 14) The flaw in Respondents' argument is that it ignores the *mens rea* requirement of § 1955(a). The crime of owning an illegal gambling business requires proof of criminal intent. *United States v. Ables*, 167 F.3d 1021, 1031 (6th Cir. 1999). Because of the *mens rea* requirement, Petitioners' interpretation of § 1955(a) poses no danger that innocent investors

will unwittingly be rendered felons. The complaint alleges that Respondents acted with knowledge that the off-shore gambling companies in which they invested millions of dollars of investors' money were flouting U.S. law.

Finally, the statute makes no exception for illegal gambling companies that trade on foreign stock exchanges. Respondents' proposed judicially created loophole would effectively legitimize off-shore havens for illegal conduct.

CONCLUSION

The Court should grant review.

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Respectfully submitted,

THOMAS I. SHERIDAN, III
Counsel of Record
ANDREA BIERSTEIN
HANLY CONROY BIERSTEIN
SHERIDAN FISHER & HAYES, LLP
112 Madison Avenue
New York, NY 10016-7416
(212) 784-6404
tsheridan@hanlyconroy.com
abierstein@hanlyconroy.com

Attorneys for Petitioners